

18-DEPARTMENT OF ADMINISTRATIVE AND FINANCIAL SERVICES

125 BUREAU OF TAXATION

CHAPTER 203 CAPITALIZATION RATE FOR TREE GROWTH TAX LAW -1997 AND 1998

SUMMARY: Implements the statutory requirement that the State Tax Assessor determine the capitalization rate each even-numbered year by use of a well-defined procedure considering all relevant factors.

A. History

The Maine Legislature in 1977 amended the Tree Growth Tax Law to require the periodic review and determination of the capitalization rate utilized in the law rather than the 10% capitalization rate originally established by statute. Previous determinations in 1978, 1980, 1982, 1984, 1986, 1988, 1990, 1992 and 1994 provided for a review of forest land market transactions, an analysis of alternative investment yields, the construction of a capitalization rate based on historic and predicted returns, and a comparative analysis of Florida Is Greenbelt Law.

B. 1996 Determination

A review of previous capitalization rate determinations and consideration of the following factors is the basis for the 1996 determination.

- (1) Market Transactions Computation of Capitalization Rate on Forest Land Investment
- (2) Comparison of an After Tax Real Capitalization Rate to Forest Land Investment
- (3) Long Term Interest Rates

Analysis of these factors exhibit results which are reasonably consistent with those of prior determinations. Details of the current analysis are available in a report prepared by Thomas E. Walker of the Property Tax Division entitled: A Review of the Capitalization Rate Used in Maine's Tree Growth Tax Law, December 1995.

The report's findings can be summarized as follows:

1. The imputed capitalization rate, which was developed from screening 1,021 forest land sales from late 1991, to 1994 was 2.9%. This compares to 3.1, 3.7, 3.8, 4.0, 3.1, 2.4, and 2.3 for

previous studies. The range of capitalization reflects the market forces acting on forest land investment in years of relatively low inflation, and moderating real estate values. A correlating study of market sales breaks the forest investment into two parts (return of growth of forest products and the investment in the real estate land) ; the table shows the sales price per acre an owner would assign to each part of the investment given varying rates of return.

2. The statewide average value per acre of harvestable timber growth by forest type decreased 32% from the reported prices obtained in 1994. This increase is offset by a rate of inflation of 2.4%/year. Despite the marked rise in the value of stumpage prices the average sales per acre decreased 5.38%.
3. The after tax capitalization rate most comparable to today's economy varies from 1.9% to 18.5% for individuals and 2.7% to 23.1% for corporations, depending on the assumed expense ratio. This method of computing a capitalization rate reduces the per acre valuation (PG) by taxes, capital costs, expenses, and risks such as forest fire before computing a capitalization rate.
4. Long term interest rates were relatively constant over the past three years and only recently inched downward. Inflation measured by the CPI is 2.4% which is a nominal pullback from the past two years.

The symmetry of this review and previous reviews is a compelling cause to neither raise nor lower the rate from 1994. Therefore, the capitalization rate of 8.5% is retained.

Effective Date.

This rule shall be effective for the State Tax Assessor's 100% valuation per acre for each forest type for each region for tax years 1997 and 1998.

STATUTORY AUTHORITY: 36 M.R.S.A. §576-B

EFFECTIVE DATE: February 5, 1980

AMENDED: February 6, 1982
February 6, 1984
February 3, 1986
January 24, 1988
February 1, 1991
October 26, 1992

June 13, 1994
September 1, 1995

EFFECTIVE DATE (ELECTRONIC CONVERSION): May 1, 1996